Team R23

Docket No. 22-123

IN THE

Supreme Court of the United States

FORDHAM PUBLIC EMPLOYEES INVESTMENT FUND, INC.,

Petitioner,

V.

KATIE GORDON, et al.,

Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Fourteenth Circuit

BRIEF FOR RESPONDENT

QUESTIONS PRESENTED

1. Whether an individual who neither "makes" nor distributes false or misleading statements can be subject to primary liability as a "disseminator" under Rule 10b-5(a) and (c), for instructing an employee to distribute the statements to investors.

2. Whether the rebuttable presumption of reliance under *Affiliated Ute* applies where the plaintiff asserts "mixed" allegations involving both omissions and affirmative misrepresentations.

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INTRODUCTION

This case is about how far private litigants should be able to reach into the decision-making process of businesses all over America. Respondent Katie Gordon, a midlevel executive at a manufacturing firm, faces the prospect of liability to private litigants for following the directions of her superiors. And, if this Court disagrees with the court below about the presumption of reliance, these litigants would not even have to prove that they relied on affirmative statements made by Ms. Gordon. To prevent private litigants from being able to overcorrect management decisions with the benefit of hindsight, this Court should find that Ms. Gordon is not liable as a primary violator and that Petitioner is not entitled to a presumption of reliance.

STATEMENT OF THE CASE

Grace Underwood and Danielle Scott met at a conference for young women in business in 2014. R. at 1. Shortly thereafter, they decided to pool their inherited wealth, over $50 million total, to acquire a small or mid-size manufacturing company. R. at 1–2. After three years of searching, they found a larger manufacturing firm that was looking to sell its machine tool business. R. at 2. Ms. Underwood and Ms. Scott would eventually acquire the business and name the spun-off entity "Gemstar." R. at 3.

Before Ms. Underwood and Ms. Scott acquired Gemstar's underlying assets, they retained an engineering firm to conduct an analysis of those assets, including the property and equipment produced there. R. at 3. That firm found trade literature indicating that the composite used by the business's largest selling machine had characteristics that could lead to microscopic cracks under stress. R. at 3. With this information included in the final report, Underwood and Scott went forward with their decision to acquire those assets and form Gemstar. R. at 3.

Underwood and Scott became CEO and President respectively, and they would together share responsibility for making "all material executive decisions." R. at 3. In just three years, Gemstar grew and became a "substantial presence in the sophisticated machine tool business." R. at 4. The focal point of Gemstar's production and sales was the SwiftMax, a production tool used to make composite materials integrated in various structural applications, including in cargo jet airplane construction. R. at 4.

Within a few years, Ms. Underwood and Ms. Scott decided that they were ready to move on and no longer wanted to hold their full interest in Gemstar. R. at 4. In January 2021, they met with Allison Ritter, a Junior Managing Director at Carter Capital with experience in mid-market mergers and acquisitions. R. at 4. In February 2021, Ritter suggested that 80% of Gemstar be sold in a private placement to institutional investors. R. at 4–5. Ms. Underwood and Ms. Scott agreed to retain 20% of Gemstar and move forward with private placement. R. at 5.

Respondent Katie Gordon served as Gemstar's Vice President of Investor Relations when Ms. Underwood and Ms. Scott began to pursue the private placement. R. at 5. She was charged with overseeing the production of the Private Placement Memorandum ("the Memo") which would be distributed to prospective Gemstar investors. R. at 5. Ms. Gordon's tasks included coordinating the various experts—accountants, engineers, attorneys, and others—who were preparing the substance of the Memo. R. at 5. Ultimately, she was responsible for managing the "flow of information" to institutional investors. R. at 5.

In May of 2021, the engineering firm consulted as one of those experts delivered to Ms. Gordon a report on the structural integrity of Gemstar's assets and products ("the Report"). R. at 5. The Report contained a memorandum written by a former employee ("the Trade Letter") outlining potential issues with the composite produced by SwiftMax, echoing the concerns raised during the original acquisition about the development of microscopic cracks. R. at 3, 5–6.

Ms. Gordon timely brought the Trade Letter to the attention of Ms. Scott and Ms. Underwood. R. at 6. Underwood concluded that the letter was outdated and written in error. R. at 6. Although Ms. Scott wondered whether to send it to auditors for review, Ms. Underwood asserted that the letter should be removed from the Report and Scott ultimately agreed. R. at 6. Following these instructions, Ms. Gordon removed the Trade Letter from the Report.

The Memo was completed in August 2021. R. at 6. The Memo made no reference to any of the issues raised regarding the SwiftMax composite. R. at 6. Ms. Gordon instructed one of her associates to send the Memo to several large financial institutions. R. at 6. The Memo included a cover page printed on Gemstar stationery and did not invite questions or note Ms. Gordon's involvement in its production. R. at 6.

In October 2021, Petitioner Fordham Public Employees Investment Fund ("the Fund") purchased 3,000,000 Gemstar shares at $27 per share as part of the private placement. R. at 7. The record does not indicate whether anyone at the Fund was aware of or read the Memo. R. at 7.

In December 2021, a cargo plane experienced an explosion while taxiing at Kennedy Airport in New York City. R. at 7. An FAA investigation into the incident revealed that failures in the fasteners securing one of the engines to the plane's wing caused the explosion. R. at 7. The fasteners at issue were produced by one of Gemstar's customers using the SwiftMax. R. at. 7. After the FAA released its findings in February 2022, the Fund sold its position in Gemstar at $4 per share, $68,000,000 below the total original purchase price. R. at. 7.

The Fund then filed this action seeking damages from Gemstar, Ms. Underwood, Ms. Scott, and Ms. Gordon "in connection with the purchase of its common stock in reliance on allegedly false and misleading statements and material omissions contained in the Memo." R. at 8. The Fund pointed to three statements made in the Memo: (1) "Gemstar's physical assets are in reasonable condition for their intended use," (2) None of Gemstar's products are materially defective," and (3) "There are no material undisclosed contingent reliabilities relating to Gemstar's products." R. at 8.

SUMMARY OF THE ARGUMENT

The conduct in this case falls outside the scope of primary liability under Section 10(b) and Rule 10b-5 and thus is not subject to Section 10(b)'s implied private right of action. Ms. Gordon did not “make” the statements at issue because she did not have ultimate authority over the statements as required by *Janus Capital Group, Inc. v. First Derivative Traders.* Ms. Gordon did not “disseminate” the statements at issue under this Court’s holding in *Lorenzo v. Securities and Exchange Commission* because she assisted in the preparation and origination of the statements and did not forward statements already made as an independent third party. Thus, she cannot be held primarily liable for violating Rule 10b-5(a) or (c) based on *Lorenzo* alone.

This Court has yet to adopt a rule delineating what conduct may give rise to primary liability under subsections (a) and (c). The only established rule post-*Lorenzo* comes from the Second Circuit, which held in *Securities and Exchange Commission v. Rio Tinto, plc* that defendants are only liable under those subsections in misstatements and omissions cases where their conduct constitutes “something beyond” misstatements and omissions. Applying the *Rio Tinto* rule to this case reveals that Ms. Gordon’s only conduct involved statements and omissions related to those made by Gemstar and not deceptive or fraudulent conduct “beyond” those statements and omissions. Ultimately, Ms. Gordon’s actions constitute at most a potential secondary violation of Rule 10b-5 and thus are only subject to legal action initiated by the SEC, not private plaintiffs.

Adopting the *Rio Tinto* standard and applying it to Ms. Gordon’s case is consistent with this Court’s precedents and maintains judicial deference to Congress’s role in securities regulation. After this Court found a private right of action under Section 10(b)-5, it explicitly limited that right of action to primary violators in *Central Bank of Denver v. First Interstate Bank of Denver*. Congress had the opportunity to expand the private right of action to secondary violators when it enacted the Private Securities Litigation Reform Act ("PSLRA"). It declined to do so. To preserve the narrowness of the implied right of action, this Court has sought to clearly distinguish primary and secondary violators. The *Rio Tinto* standard continues in this tradition, providing an administrable rule defining primary and secondary Rule 10b-5(a) and (c) violations while maintaining deference to Congress's role in defining private rights of actions and dividing enforcement authority between private parties and the SEC.

The Fund is also not entitled to the presumption of reliance recognized by *Affiliated Ute*. Lower courts have mostly confined the application of this presumption to cases that primarily involve omissions. A case is not one that primarily involves omissions if the alleged omissions are just the inverse of affirmative statements at issue. The confinement of the presumption to cases of primarily omissions makes sense because the rationale for the presumption is that the plaintiff shouldn't have to prove a speculative negative and this is not the task that a plaintiff faces when they have affirmative statements that they can prove they relied on.

ARGUMENT

I. THIS COURT SHOULD REVERSE THE CIRCUIT COURT'S FINDING THAT MS. GORDON IS SUBJECT TO PRIMARY LIABILITY BECAUSE SHE DID NOT ENGAGE IN CONDUCT "BEYOND" THE STATEMENTS AND OMISSIONS AT ISSUE.

Section 10(b) of the Securities Exchange Act prohibits the use of any "manipulative or deceptive device" in connection with the purchase or sale of securities and empowers the SEC to promulgate rules enforcing this prohibition. 15 U.S.C. § 78j(b). Rule 10b-5 makes it unlawful to "employ any device, scheme, or artifice to defraud," "make any untrue statement of material fact . . . or omit to state a material fact" or "engage in any act, practice, or course of business which operates . . . as a fraud" in connection with a security transaction. 17 C.F.R. § 240.10b-5(a)–(c).

Private plaintiffs only have an implied right of action against primary violators of Rule 10b-5. *See Cent. Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, 511 U.S. 164, 177–78 (1994). Ms. Gordon's conduct does not give rise to primary liability under Rule 10b-5(b) because she did not "make" the allegedly misleading statements. *See Janus Cap. Grp. v. First Derivative Traders, Inc.*, 564 U.S. 135, 142 (2011) (holding that a party only "makes" a statement under Rule 10b-5(b) where they have "ultimate authority over the statement.").

This court must thus determine whether Ms. Gordon's conduct gives rise to primary liability under either of the other two subsections, Rule 10b-5(a) and (c). This Court has not clearly defined primary liability under these subsections, which is also known as "scheme liability." In *Lorenzo v. Securities*

& Exchange Commission, this Court determined that a "dissemination" of false or misleading information can be a basis for scheme liability. 139 S. Ct. 1094, 1100 (2019). The Court recognized that application of its more expansive reading of these subsections would be difficult to apply in "borderline" cases. *Id.* at 1101. But the Court does not delve into details, noting only that "purpose, precedent, and circumstance" may limit *Lorenzo*'s application. *Id.*

Only one federal court has sought to fashion a rule governing scheme liability claims since *Lorenzo*. In *Securities and Exchange Commission v. Rio Tinto, plc*, the Second Circuit held that a defendant can only be primarily liable under scheme liability where the alleged conduct includes "something beyond" misstatements and omissions. 41 F. 4th 47, 49 (2d Cir. 2022). Accordingly, the "dissemination" of misstatements in *Lorenzo* serves as an example of conduct that satisfies this "something beyond" requirement. *See id.* The rule fashioned by *Rio Tinto* accords with pre-*Lorenzo* caselaw in the Second Circuit and other circuit courts. *See Lentell v. Merril Lynch & Co.*, 396 F.3d 161, 177–78 (2d Cir. 2005) (finding that plaintiffs could not state a market manipulation claim under Rule 10b-5(a) or (c) where the "sole basis" for those claims was misrepresentations and omissions); *W. Va. Pipe Trades Health & Welfare v. Medtronic, Inc.*, 845 F.3d 384, 392 (8th Cir. 2016) (holding that scheme liability requires plaintiffs to "allege some deceptive act other than the fraudulent misrepresentation."); *WPP Luxembourg Gama Three Snarl v. Spot Runner, Inc.*, 655 F.3d 1039, 1057 (9th Cir. 2011) (requiring a claim under scheme liability to "encompass[] conduct beyond . . . misrepresentations and omissions.").

Under *Lorenzo* as interpreted by *Rio Tinto*, Ms. Gordon did not "disseminate" the statements at issue because her conduct primarily involved preparation and origination of the statements, not the separate sharing of statements already made by another party. The court below erred when it found Ms. Gordon to be a primary violator because it failed to differentiate between her preparation and origination of the statements here the dissemination at issue in *Lorenzo*. Further, no other action by Ms. Gordon rises to this "something beyond" standard: she committed no deceptive or fraudulent act separate from and beyond the preparation of and assistance in making the statements at issue. In finding that Ms. Gordon's conduct does not subject her to primary scheme liability, this Court should hold that its ruling in *Lorenzo* is subject to the "something beyond" requirement as expressed in *Rio Tinto*. This requirement allows this Court to maintain fidelity to its prior decisions and Congressional intent. Ms. Gordon is not a primary violator under any subsection of Rule 10b-5 and enforcement of the securities laws in her case belongs to the Commission, not private parties.

A. Ms. Gordon's conduct does not subject her to primary liability because she did not "disseminate" the Memo nor engage in any other conduct "beyond" the statements and omissions at issue

Ms. Gordon cannot be held liable under scheme liability because her actions ultimately constitute the preparation of alleged misstatements and not distribution or dissemination of the same. Further, Ms. Gordon's position at Gemstar speaks only to her scienter and liability as the "maker" of the statement under *Janus*, not her liability as a disseminator.

(i) Ms. Gordon's conduct does not constitute "dissemination" under Lorenzo or Rio Tinto because she acted to help Gemstar originate its alleged misstatements without distributing them in her own capacity

Creating and "making" statements on behalf of another is conduct distinct from disseminating statements. *Lorenzo* involved an investment bank director who knowingly forwarded false statements by a client firm to potential investors. *Lorenzo*, 139 S. Ct. at 1100. The Court noted that although Lorenzo did not "make" the false statements in violation of Rule 10b-5(b), his dissemination of those statements still fell within the scope of the other subsections. *Id.* The conduct this Court classified as dissemination in Lorenzo does not describe Ms. Gordon's conduct; thus, she cannot be held primarily liable as a "disseminator."

As the Second Circuit noted in *Rio Tinto*, *Lorenzo* did not "go so far as to create primary liability for participation in the preparation of misstatements." 41 F.4th at 54 (internal quotations and citations omitted). When Lorenzo shared his client's false statements with prospective investors, he identified himself as the author of those emails and invited the recipients to inquire further about the investment opportunity he was advertising. *Lorenzo,* 139 S. Ct. at 1099. Lorenzo's emails were not the origin of the false statements—his client had made the same misrepresentations three months prior in public filings. *Id.* In essence, Lorenzo took misrepresentations that had already been made, and "disseminated" them by spreading the information in his capacity as an outside financial advisor and expert.

Ms. Gordon's communications at issue here are inapposite to Lorenzo's. Ms. Gordon did not "disseminate" under her own banner statements that had already been made. When she instructed her associate to send the Memo to potential investors, Ms. Gordon merely *facilitated* the making of the statements by Gemstar, as evidenced by the use of Gemstar company stationery for the Memo's cover letter and lack of any reference in the cover letter to Ms. Gordon's role in creating the Memo. *See Janus*, 564 U.S. at 142–43 ("And in the ordinary case, attribution within a statement or implicit from surrounding circumstances is strong evidence that a statement was made by—and only by—the party to whom it is attributed.").

This "distribution" rather than "dissemination" of statements cannot give rise to scheme liability under Rule 10b-5. Under *Rio Tinto*, Lorenzo's email to investors on his own behalf containing misstatements already made satisfies the "something beyond" requirement for liability. *See* 41 F.4th at 49. The court below identifies Ms. Gordon's instruction to her associate to distribute the Memo as that "something," but fails to identify the separation between that conduct and the making of potentially misleading statements by Gemstar. *See* R. at 16–17. That instruction was not "something beyond" the statements of Gemstar but were an essential step in the making of the statements.

(ii) Ms. Gordon's conduct does not otherwise constitute "something beyond" under the Rio Tinto *standard.*

The court below suggests that some of Ms. Gordon's conduct other than her role in distributing the Memo may give rise to scheme liability. The only other identifiable actions beyond the alleged "dissemination" of misstatements are the concealment of the Trade Letter from both potential auditors and Gemstar's experts. Neither of these courses of conduct constitute "something beyond" the misstatements at issue because they are not sufficiently distinguishable from the final misstatements at issue in this case.

Lorenzo did not define specifically what kind of conduct could create scheme liability beyond the facts of that specific case. The *Rio Tinto* analysis of "something beyond" misstatements does not itself provide additional context. The court below answered affirmatively the question posed by *Rio Tinto* regarding whether interfering with or corrupting an audit gives rise to scheme liability but provided little further guidance. R. at 17.

Courts that applied similar standards prior to *Lorenzo* and *Rio Tinto* have found that conduct relating to misstatements or omissions constituted "something beyond" where that conduct was deceptive and was *not* making or preparing misstatements and omissions. In *Medtronic*, the Eighth Circuit found that defendant had participated in a scheme under Rules 10b-5(a) and (c) where it paid doctors to publish false information about its medical products in medical journals. 845 F.3d 384, 393 (8th Cir. 2016). One district court has also found scheme liability where defendants created "shell" companies to hide expenses and to overstate revenue, which led to misstatements and omissions. *See In re Lernout & Hauspie Sec. Litig.*, 236 F. Supp. 2d 161, 173 (D. Mass. 2003). Here, unlike in these cases, Ms. Gordon's conduct only constituted omissions, statements, and acts preparing subsequent statements and omissions.

The Fund may assert that under *Rio Tinto*, Ms. Gordon participated in the "plan" to defraud investors by failing to disclose the Report to Gemstar's experts. Arguably, the failure to share information with the experts constitutes something beyond the statements made by Gemstar and creates a source of primary liability. But this theory fails for several reasons. First, just as Ms. Gordon was not ultimately responsible for the contents of the Memo, the contents of the Report appeared to be subject to the final approval of Ms. Underwood and Ms. Scott. *See* R. at 6. *Janus*'s definition of who "makes" a statement in the context of a Rule 10b-5(b) violation should be equally controlling here as in the context of the Memo because holding otherwise would subject Ms. Gordon to primary liability for statements she did not make under Rule 10b-5(b) based on other statements she did not make. *See Janus*, 564 U.S. at 142–43. Ms. Gordon merely participated in the preparation of the Report, just as she merely participated in the preparation of the Memo.

Second, the action of editing the Report to not include the Trade Letter is itself an omission preceding the statements alleged to be misleading here. The "something beyond" misstatements and omissions requirement for scheme liability cannot be satisfied by alleging further misstatements and omissions. *See Rio Tinto*, 41 F.4th at 53 (affirming dismissal of a complaint characterized by the district court as "a collection of misstatements and omissions"). Where the fraudulent conduct conducted pursuant to a 10b-5(b) violation is in essence another 10b-5(b) violation, scheme liability remains inappropriate. Beyond the "dissemination" example in *Lorenzo*, other instances of scheme liability involve fraudulent acts that do not constitute misstatements or omissions. The Eighth Circuit relied on the payments to doctors as "something beyond" in *Medtronic*, and the District of Massachusetts relied on the establishment of shell companies in *In re Lernout*. *See* 845 F.3d at 394; 236 F. Supp. 2d at 173. While these deceptive acts were ultimately in service of misstatements, they were not themselves misstatements and those engaged in those acts were not merely writing, preparing, or producing the statements at ultimate issue in those cases. Ms. Gordon's removal of the Trade Letter from the Report is merely an omission, the objects of which are the statements made later in the Memo, not "something beyond" the alleged misstatements at issue in this case.

Finally, finding the omission of the Trade Letter to be "something beyond" would be inconsistent with this Court's holding in *Stoneridge*. There, this Court refused to find a private right of action under Rule 10b-5 against a party who "committed a deceptive act in the process of providing assistance." *Stoneridge*, 552 U.S. at 162. Ms. Gordon's omission of the Trade Letter aided Gemstar's misstatements to potential investors. Thus, she cannot be a primary violator based on this conduct under *Stoneridge*, and finding otherwise would "revive in substance the implied cause of action against all aiders and abettors." *Id.*

Lorenzo did not overrule this key principle. The deceptions in *Stoneridge*—like Ms. Gordon's removal of the Trade Letter—did not and could not engender reliance from the investing public. *See Stoneridge*, 552 U.S. at

159. Conversely, Lorenzo knowingly emailed misstatements to potential investors; his deception was directed at, rather than hidden from, the investing public. *See Lorenzo*, 139 S. Ct. at 1104. In *Medtronic*, the defendant's actions themselves were deceptive and defrauded the investing public by misrepresenting the independence of important clinical trials. *See* 845 F.3d at 394. This deception about the validity of misstatements is like Lorenzo's deceptions, and unlike the omissions Ms. Gordon made to the Gemstar experts, which ultimately were reflected in the Memo.

(iii) Job titles and awareness of potential misstatements do not bear on whether Ms. Gordon's conduct gives rise to scheme liability.

The Fund may argue that Ms. Gordon's agency and position in Gemstar's organizational hierarchy justifies subjecting her to primary scheme liability. However, such a finding speaks primarily to the scienter requirement, and not to whether her conduct falls within the scope of the scheme liability provisions.

In finding Ms. Gordon primarily liable, the court below distinguishes her from her associate, who they say only acted as a "mailroom clerk" with respect to the Memo. R. at 17 (quoting *Lorenzo*, 139 S. Ct. at 1103). This language draws on a distinction made by this Court in *Lorenzo*, citing mailroom clerks as a category of persons "tangentially involved in dissemination . . . but for whom liability would be inappropriate." *Lorenzo*, 139 S. Ct. at 1103. Despite this distinction, this Court has characterized questions of liability under Rule 10b-5 as concerning the conduct of the defendant. *Id.* (describing the ruling as "applying subsections (a) or (c) of Rule 10b-5 to *conduct* like [Lorenzo's].") (emphasis added).

A defendant's position or role in a firm may speak to their ultimate authority over a statement and their primary liability under Rule 10b-5(b). *See Janus*, 564 U.S. at 142–43. However, the court below rejected this primary liability, and the fact that Ms. Gordon did not make the statements in this case is not at issue here. *See* R. at 14, 30.

The difference between Ms. Gordon and her associate or a Gemstar mailroom clerk is simply one of knowledge, not conduct. Ms. Gordon concededly knew that the Trade Letter was excluded from the Memo; the record does not reflect whether her associate shared this knowledge. However, nothing about Ms. Gordon's *conduct* sufficiently distinguishes her from her associate. She was instructed by her superiors to remove the Report and ensure the Memo reached potential investors, and she instructed her associate similarly. Her more than tangential "involvement" in the decision—which ultimately belonged to her superiors—to make the statements at issue could speak to her potential scienter or intention to aid and abet a potential violation. Her job title at Gemstar does not increase the scope of conduct subject to liability under Rule 10b-5, which ought to be governed by the principles enunciated in *Lorenzo* and *Rio Tinto*. Guided by those principles, this Court should find that Ms. Gordon is not a primary violator and affirm the dismissal of the complaint against her.

B. This Court's precedents and deference to Congressional authority require this Court to adopt the Rio Tinto standard for scheme liability.

This case presents the Court an opportunity to render a blurry line clear. The text of Rule 10b-5 and this Court's precedents demand an affirmation that scheme liability requires "something beyond" misstatements and omissions. Further, that "something" must be an act sufficiently distinct from the making of material statements to give rise to primary liability.

(i) The history of both Congressional action on and judicial interpretation of private Rule 10b-5 actions demand the clear distinction Rio Tinto provides between primary and secondary scheme liability

The texts of Section 10(b) and Rule 10b-5 do not grant private parties any rights or remedies. This Court has found an implied right of action under Section 10(b) but has unequivocally limited it to primary violators of Rule 10(b)-5. *See Central Bank*, 511 U.S. at 177–78. The *Central Bank* court found two independent justifications for its decision to exclude aiders and abettors from this implied right. First, the court finds that the texts of Section 10(b) and Rule 10b-5 do not cover the conduct of secondary violators. *Id.* While the statutory text does apply to those who "directly and indirectly engage" in the conduct proscribed therein, the Court defines aiding and abetting liability as covering those who provide aid without even indirectly engaging in the proscribed conduct. *Id.* (quoting 15 U.S.C. § 78j(b)). Second, the Court noted that in other portions of the securities laws where Congress *had* granted an explicit right of action, it did not include liability for aiding and abetting liability. *Id.* at 179–80. Both findings led the Court to construe the implied right of action narrowly and exclusive of secondary violators.

Following *Central Bank*, Congress enacted the Private Securities Litigation Reform Act of 1995 ("PSLRA"), affirming the SEC's exclusive role in actions against aiders and abettors. *See* 15 U.S.C. § 78t(e). Prior to the law's passage, the Commissioner of the SEC recommended that Congress include a private right of action against secondary violators. *See* S. Hearing. No. 103-759, pp. 13–14 (1994). This Court has interpreted Congress' failure to include such a provision in the PSLRA as affirmation of the narrow definition it gave to the implied right of action under § 10(b). *See Stoneridge Inv. Partners, LLC v. Scientific-Atlanta*, 552 U.S. 148, 157–58 (2008).

This vital distinction between primary and secondary liability survived the *Lorenzo* decision. *See Lorenzo*, 139 S. Ct. at 1103–04. Thus, the main question this Court must consider is whether those actions can subject her to liability in the context of the "narrow dimensions" of the private right of action against primary violators. *Stoneridge*, 552 U.S. at 167. Maintaining the conservative nature of the implied right of action as this Court and Congress have both directed requires drawing "clean line[s]" between primary and secondary liability. *Janus*, 564 U.S. at 143 n.6 (noting that distinction between primary and secondary liability is necessary to give effect to the *Central Bank* decision).

The Second Circuit's decision in *Rio Tinto* correctly draws this line because it creates an intelligible and administrable rule consistent with this

Court's decisions and Congress's design of the securities law enforcement regime. Scheme liability requires acts beyond misstatements and omissions, and "*Lorenzo* tells us that dissemination is one example of something extra that makes a violation a scheme." *Rio Tinto*, 41 F.4th at 54. This argument does not conflict with the *Lorenzo* decision. *Lorenzo* rejected the argument that the subsections of Rule 10b-5 govern mutually exclusive categories of conduct. *See* 139 S. Ct. at 1102. Under *Rio Tinto*, misstatements or omissions can still be central to a fraudulent scheme or course of business as defined under the Rule. But primary scheme liability should require fraudulent or deceptive conduct that goes beyond merely aiding in the creation of misstatements.

(ii) Rio Tinto's standard of "something beyond" misstatements and omissions is necessary to give effect to this Court's holding in Janus.

A decision *rejecting* the standard laid out in *Rio Tinto* would render this Court's holding in *Janus* moot. There, this Court held that only those with "ultimate authority" over a statement can "make" such statement for purposes of Rule 10b-5(b) liability." *Janus*, 564 U.S. at 142–44. An independent outside entity who helped prepare the fraudulent prospectuses at issue could thus only be subject to secondary liability, which does not fall within the private right of action. *Id.* The *Rio Tinto* standard for scheme liability would lead to the same result. There was preparation and assistance in making statements, but not fraudulent or deceptive action "beyond" the statements. Without the *Rio Tinto* rule and under the Fund's theory of scheme liability, the independent advisor in *Janus* would be subject to scheme liability based on its conduct, washing away the "narrow dimensions" this Court sought to give primary liability under 10b-5. *Janus*, 564 U.S. at 142 (quoting *Stoneridge*, 552 U.S. at 167.

The court below attempts to distinguish Ms. Gordon's actions from the independent advisor in *Janus* by noting that she delivered the Report to experts and instructed her associate to distribute the Memo. R. at 16. While the outside advisor in *Janus* did not deliver the prospectus to investors or other interested groups, they could still have been found liable for scheme liability given their "more than tangential" involvement in the misrepresentations at issue there. *See Janus*, 564 U.S. at 147–48 (noting that the independent advisor was "significantly involved" in authoring the misstatements at issue). In *Lorenzo* this court affirmed the *Janus* rule that someone who helps draft a statement does not commit a primary violation of rule 10b-5(b). *Lorenzo*, 139 S. Ct. at 1103. Adopting *Rio Tinto* allows this Court to preserve the distinction made between primary and secondary violators while further defining the contours of scheme liability.

(iii) Respect for Congress as the primary delineator of securities law violations and remedies requires adopting the Rio Tinto standard.

A careful distinction between the conduct barred by the various subsections of Rule 10b-5 respects the will of Congress regarding private 10b-5 actions. When Congress enacted the PSLRA, it not only rejected a codified right of action against aiders and abettors but also instituted heightened pleading standards for private actions brought based on misstatements or omissions. 15 U.S.C. § 78-u4(b)(1). Complaints alleging scheme liability are not subject to this heightened standard, because those subsections do not require the allegation of any misleading statement or omission. *See Rio Tinto*, 41 F. 4th at 52. Abrogating *Janus* and failing to limit the scope of *Lorenzo* would allow plaintiffs to recast misstatement and omissions cases as scheme cases and circumvent the standards Congress imposes on those actions.

At a broader level, expanding the universe of private securities actions that plaintiffs are able to bring would run counter to Congress's clear intent in passing the PSLRA. As noted previously, Congress has not sought to correct this Court's rejection of private actions under Rule 10b-5 against secondary violators. *See Stoneridge*, 552 U.S. at 165–66. The PSLRA intended not just to affirm this limitation, but generally "deter frivolous lawsuits brought by private plaintiffs." H.R. Conf. Rep. No. 104-396, at 32 (1995). This Court has since concluded that the enactment of PSLRA illustrates Congress's skepticism towards private securities litigation. *See Stoneridge*, 552 U.S. at 164 ("It is appropriate for us to assume that when [the PSLRA] was enacted, Congress accepted the § 10(b) private cause of action as the defined but chose to extend it no further."). Adopting the *Rio Tinto* standard for scheme liability ensures that the decision to expand the judicially created private right of action remains with Congress. *See id.* at 165.

In concluding that private action can reach Ms. Gordon's conduct, the circuit court argues that such allowance is vital to securities law enforcement, arguing that they otherwise "do not see how the securities laws can achieve a high standard of business ethics in the securities industry." R. at 15 (internal quotations and citations omitted). However, no argument Ms. Gordon presents here precludes the SEC from pursuing enforcement against her or a similarly situated party. As discussed, the division of securities law enforcement between the SEC and private litigation is ultimately governed by Congress. The question before the Court concerns exclusively the viability of private suits, in fidelity with precedent and Congressional intent, against individuals who participate in the production false or misleading statements under a theory of scheme liability.

II. THIS COURT SHOULD AFFIRM THE CIRCUIT COURT'S FINDING THAT THE FUND HAS NOT PLED RELIANCE BECAUSE THE PRESUMPTION OF RELIANCE RECOGNIZED BY *AFFILIATED UTE* DOES NOT APPLY IN CASES THAT INVOLVE ALLEGATIONS OF BOTH AFFIRMATIVE MISREPRESENTATIONS AND OMISSIONS.

A plaintiff bringing a 10b-5 action must show that they relied on the alleged misrepresentation. *See Stoneridge Inv. Partners, LLC v. Scientific-Atlantica*, 552 U.S. 148, 157 (2008). In *Affiliated Ute Citizens of Utah v. United States*, this Court recognized a presumption of reliance where the case "involved primarily a failure to disclose" and the facts withheld were "material in the sense that a reasonable investor might have considered them important in" making the transaction in question. 406 U.S. 128, 153–54 (1971) . This case does not primarily allege an omission, nor does it involve any of the circumstances that warranted the presumption in *Affiliated Ute*. This Court should thus affirm the Circuit Court's holding that the presumption of reliance does not apply here. The Fund has not pled the element of reliance and the motion to dismiss should be granted in favor of Ms. Gordon.

A. The presumption of reliance does not apply here because it applies only where a plaintiff primarily alleges omission of material information by someone with a duty to disclose.

Reliance should not be presumed in this case because the Fund does not primarily allege an omission. This court recognized a presumption of reliance applicable to 10b-5 cases in *Affiliated Ute*. 406 U.S. at 153. In that case, two bank employees responsible for handling shares of tribal assets actively cultivated a secondary market that yielded more value for the shares. *Id.* at 146. Because they did not tell the tribal shareholders about the prices being paid for the shares in this market, the bank employees were able to buy the shares cheaply from the tribe members and then sell them to nonmembers for undisclosed profit. *Id.* Under these circumstances, this Court held that positive proof of reliance was not required where (1) the case involved "primarily a duty to disclose" and (2) "the facts withheld [are] material in the sense that a reasonable investor might have considered them important in the making of this decision." *Id.* at 153-54. The court reasoned that the bank employees "*may not stand mute* while they facilitate the mixed-bloods' sales to those seeking to profit in the non-Indian market *the defendants had developed and encouraged* and with which they were fully familiar." *Id.* at 153 (emphasis added).

This Court has not since had a chance to further develop the doctrine around this presumption, but lower courts have developed an analysis to determine whether a case is primarily one of omission before applying the *Affiliated Ute* presumption. *See Binder v. Gillespie*, 184 F.3d 1059, 1064 (9th

Cir. 1999) (concluding that "the preferred approach" among circuit courts is to "analytically characterize the action as either primarily a nondisclosure case (which would make the presumption applicable), or a positive misrepresentation case.") (internal quotation marks omitted) (citing *Finkel v. Docutel/Olivetti Corp.*, 817 F.2d 356, 359 (5th Cir. 1987)). A case is not primarily one of omissions if the alleged omissions are just the inverse of available affirmative statements. *See Starr ex rel. Estate of Sampson v. Georgeson Shareholder, Inc.*, 412 F.3d 103, 109 n.5 (2d Cir. 2005) (finding that the *Affiliated Ute* presumption did not apply where the alleged omissions merely "exacerbated the misleading nature of affirmative statements."); *Waggoner v. Barclays PLC*, 875 F.3d 79, 96 (2d Cir. 2017) (relying on *Starr* to find that the *Affiliated Ute* presumption did not apply where the alleged omission was "simply the inverse of the Plaintiffs' misrepresentation allegation[.]"); *In re Volkswagen "Clean Diesel" Marketing, Sales Practices, & Products Liability Litigation*, 2 F.4th 1199, 1208 (9th Cir. 2021) (finding that the *Affiliated Ute* presumption did not apply where the alleged omission was "simply the inverse of the affirmative misrepresentations" at issue).

Here, any alleged omissions would just be the inverse of affirmative statements, so the case is not primarily one of omission and the presumption should not apply. The alleged omissions here are analogous to those in *Waggoner* and *In re Volkswagen*. For example, in *Waggoner*, plaintiffs alleged that the defendant failed to disclose that a protective feature of its trading platform did not apply to many of the trades made on the platform. 875 F.3d at 96. But this was just the inverse of the plaintiffs' allegation that the defendant misled investors by affirmatively stating that the platform feature protected traders. *Id.* And in *In re Volkswagen*, plaintiffs alleged that Volkswagen failed to disclose that its vehicles were equipped with devices that allowed it to misrepresent the emissions produced by those vehicles. 2 F.4th at 1207. But this was just the inverse of plaintiffs' allegation that Volkswagen's affirmative statements about environmental compliance were materially false or misleading. *Id.* at 1208. In both cases there was (1) an allegation of omitted information and (2) affirmative statements that were made misleading because of this omission.

So too here. The Fund alleges that a Trade Letter omitted from the Private Placement Memorandum amounted to nondisclosure about contingent liabilities relating to the defective composite. But the Fund also alleges three affirmative statements that may have been made misleading because of this omission: (1) Gemstar's physical assets are in reasonable condition for their intended use, (2) None of Gemstar's products are materially defective, and (3) There are no material undisclosed contingent liabilities relating to Gemstar's products. The alleged omission does not include any information that would do anything other than "exacerbate[] the misleading nature of [these] affirmative statements." *Starr ex rel. Estate of Sampson v. Georgeson Shareholder, Inc.*, 412 F.3d 103, 109 n.5 (2d Cir. 2005).

Thus, under the current prevailing analysis, the presumption of reliance should not be applied here because the alleged omissions are only the inverse of alleged affirmative misstatements.

B. Extension of the presumption is not warranted where a plaintiff alleges that specific affirmative statements were misleading.

The rationale underlying the presumption of reliance counsels against extending it to "mixed" cases that involve allegations of both omissions and affirmative misstatements. If the presumption were to be extended to such cases, "*Affiliated Ute* would become available for all securities fraud claims because all misrepresentations can be cast as omissions, at least to the extent they fail to disclose which facts are not true." *In re Volkswagen "Clean Diesel" Marketing, Sales Practices & Products Liability Litigation*, 2 F.4th 1199 (9th Cir. 2021). Because "misrepresentations" and "omissions" are two sides of the same coin, the analysis of whether to apply the presumption should be rooted in the rationale for having the presumption: "in cases like *Affiliated Ute*, *in which no positive statements exist*, reliance as a practical matter is impossible to prove." *Wilson v. Comtech Telecommunications Corp.*, 648 F.2d 88, 93 (2d Cir. 1981) (emphasis added). *See also Binder v. Gillespie*, 184 F.3d 1059, 1064 (1999) (noting that most circuits have limited the presumption to cases that primarily allege omissions because of the "difficulty of proving 'a speculative negative[.]'") (quoting *Blackie v. Barrack*, 524 F.2d 891, 905 (9th Cir. 1975)).

The presence of specific affirmative misstatements here distinguishes this case from *Affiliated Ute* in a way that makes application of the presumption unwarranted. *Affiliated Ute* involved extraordinarily unique circumstances: the securities in question represented shares of a corporation that was devised to partition and distribute tribal assets at the termination of federal supervision; tribal shareholders were compelled by statute to first offer their stock to other members of the tribe before attempting to sell to a nonmember; each stock certificate “had on its face, in red lettering, a warning that the certificate did not represent stock in an ordinary business corporation, that its future value or return could not be determined, and that the stock should not be sold or encumbered by its owner,” but rather was intended to be “retained and preserved for the benefit of the shareholder and his family;” and the bank that the defendants worked at was the exclusive transfer agent of the shares and “had physical possession of all the stock certificates with their specific legend of caution and warning.” 406 U.S. at 133–45.

These unique circumstances made shareholders entirely reliant on the bank to determine the value of these shares with a statutorily limited secondary market. *Id.* at 152 (“The mixed-blood sellers considered these defendants to be familiar with the market for the shares of stock and relied upon them when they desired to sell their shares.”) (internal quotation marks omitted). This Court also emphasized the active role that the bank employees played in developing a secondary market with higher prices. *Id.* Because there were no affirmative statements about this secondary market, without the presumption plaintiffs would have had to prove that they relied on what the defendants didn't say (the “speculative negative” referenced in *Binder*, supra).

Here, though, the Fund "alleges numerous affirmative misstatements" and "are therefore not in a situation in which it is impossible for them to point to affirmative misstatements." *Waggoner v. Barclays*, 875 F.3d at 96. Despite this material distinction, one of the dissenting opinions below analogizes this case to *Affiliated Ute* in other ways that miss the mark. Namely, the dissent analogizes Ms. Gordon to the bank employees by saying that she also "engaged in more than ministerial functions" because she instructed distribution of the Memo. R. at 29. First, it is not clear why instructing distribution of the memo is not a ministerial function; it seems to be a task ancillary to the actual representations made within the report. Secondly, when this Court in *Affiliated Ute* said that the defendants there "engaged in more than ministerial functions," it was likely referring back to the fact that the employees "developed and encouraged" the demand in the secondary market that they did not disclose to the tribal shareholders. 406 U.S. at 153; *id.* at 151–52 ("We would agree that if the two men and the employer bank had functioned merely as a transfer agent, there would have been no duty of disclosure here. But, as the Court of Appeals itself observed, the record shows that [the bank employees] 'were active in encouraging a market for the UDC stock among non-Indians.'") (internal citations omitted).

The attempt by the dissent below to analogize any fiduciary duty that Ms. Gordon might have to the Fund to that which the bank employees had in *Affiliated Ute*, R. at 29, is similarly mismatched. The "affirmative duty" in *Affiliated Ute* specifically refers to the duty of broker-dealers who are also market makers to disclose the fact that they are market makers. 406 U.S. at 153 (citing *Chasins v. Smith, Barney & Co.*, 438 F.2d 1167 (2d Cir. 1970)); *see Chasins v. Smith, Barney & Co.*, 438 F.2d 1167, 1172 (2d Cir. 1970) ("In this situation failure to inform the customer fully of its possible conflict of interest, in that it was a market maker in the securities which it strongly recommended for purchase by him, was an omission of material fact in violation of Rule 10b-5."). Ms. Gordon was not a broker-dealer-cum-market-maker in this transaction, so this circumstance of *Affiliated Ute* is similarly not present.

Finally, the Third and Tenth Circuits have pointed out administrability issues that would result from an extension of the *Affiliated Ute* presumption to "mixed" cases. As explained by the Tenth Circuit, "[i]n such 'mixed' cases, '[a] strict application of the omissions-misrepresentations dichotomy would require the trial judge to instruct the jury to presume reliance with regard to the omitted facts, [but] not to presume reliance with regard to the misrepresented facts.'" *Joseph v. Wilson*, 223 F.3d 1155, 1162 (10th Cir. 2000) (quoting *Sharp v. Coopers & Lybrand*, 649 F.2d 175, 188 (3d Cir.1981)) (abrogated on other grounds by *California Public Employees' Retirement System v. ANZ Securities, Inc.*, 137 S. Ct. 2042 (2017)). "Rather than subject the jury to such a confounding exercise," the Tenth Circuit continued, "a unitary burden of proof on the reliance issue should be set according to a context-specific determination of where that burden more appropriately lies." *Id.* (quoting *Hoxworth v. Blinder, Robinson & Co., Inc.*, 903 F.2d 186, 202 (3d Cir.1990)). Navigating this issue is not necessary where affirmative statements are available and where alleged omissions are merely the inverse of those affirmative misstatements.

For the foregoing reasons, this Court should ratify the current prevailing approach that limits the *Affiliated Ute* presumption of reliance to cases that primarily involve omissions. Cases such as this one, where any alleged omissions are the inverse of alleged affirmative misstatements, do not qualify because doing so "would permit the *Affiliated Ute* presumption to swallow the reliance requirement almost completely . . . [and] fail to serve the Affiliated Ute presumption's purpose." *In re Volkswagen "Clean Diesel" Marketing, Sales Practices, & Products Liability Litigation*, 2 F.4th at 1205–06 (quoting *Joseph v. Wilson*, 223 F.3d at 1163). The motion to dismiss should therefore be granted in favor of Ms. Gordon since the Fund has not pled reliance.

CONCLUSION

For the foregoing reasons, Ms. Gordon respectfully asks this Court to (1) reverse the finding of the court below that she is liable as a primary violator and (2) affirm the finding of the court below that the Fund is not entitled to the *Affiliated Ute* presumption. The Court should thus affirm the decision of the court below to dismiss the case.

Respectfully Submitted,
/s/ Team R23
Counsel of Record for Respondent